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SUBJECT: Reforming the Countryside: Micro-Finance in Guangxi Province

¶1. (U) Microfinance is on the rise in Guangxi, as commercial banks, rural credit unions and non-governmental organizations (NGOs) expand their lending programs. Banks are eager to make rural finance profitable. The area's dominant rural credit union complains that defaults continue to be a problem. NGOs comment that government restrictions remain tight; the balancing act is figuring out far to push the envelope in expanding operations, without clear legal or financial parameters. For now, the Guangxi government seems content to give microfinanciers space to expand but offers little support. A major expansion of microfinance in Guangxi is unlikely without significant reforms that balance both political goals, and financial growth. End summary.

Return to the Countryside! Commercial Bank Reform

¶2. (SBU) Some commercial banks are giving the rural sector a second look, thanks in part to emphasis from the central government to support its 'New Socialist Countryside' policy. In 2005, the Agricultural Bank of China - Guangxi (ABC-GX) shut down its rural micro-lending program to focus on the urban sector in an attempt to maximize profits. However, the bank renewed its commitment to rural finance in November 2007 and revived its loan program by providing loans to sugarcane farmers in Congzuo municipality and to rattan product weavers in Hechi municipality, the program's pilot sites. According to Jiang Wucheng, Assistant President of ABC-GX, the bank now views rural finance as a large market with profit potential, a vast change from the bank's previous outlook. Jiang told us that the bank's motivation has shifted from 'poverty alleviation' to 'supporting rural development,' hinting at an increasingly commercial focus.

¶3. (U) Under the new program, rather than target average households and farmers as before, lenders are giving preferential treatment to agricultural companies and "model" farmers and households (i.e. high profit producers). In the past, commercial rural credit loans for households averaged RMB 1,000 to 3,000 (about USD 150 - 440); now, loans are RMB 3,000 to 5,000 for average households and RMB tens-to-hundreds of thousands for "model" recipients. In addition, the Bank has also created new loan models such as "company + farmer" guarantees and joint warrants from multiple households to lower financial risks. From December 2007 to July 2008, the bank issued RMB 10.21 million (USD 1.5 million) in loans and 236,000 credit cards to farmers. The Bank plans to expand its programs to several additional locations throughout Guangxi by August/September 2008.

Rural Credit Unions Feel the Crunch

14. (U) Most of Guangxi's rural finance programs are administered by the Guangxi Rural Credit Union (GX-RCU). GX-RCU absorbed much of the commercial banks' rural business in the nineties when they shifted focus to the urban sector. GX-RCU issues loans to independent households and collective guarantee groups, averaging between RMB 1,000 and RMB 5,000 (USD 150 - 740), on a one-year repayment plan. For the last three years, GX-RCU has maintained the largest level of rural financial deposits in the province. Nearly one-third of Guangxi's 9.3 million households are GX-RCU clients, and it accounts for 90% of Guangxi's small credit business. Like many microfinance providers, the Guangxi Rural Credit Union also offers services in addition to micro-lending and credit -- investment advice, financial risk analysis and a youth entrepreneurship program.

15. (SBU) According to Ban Bizhong, General Manager of the GX-RCU's Credit Planning Department, the Union's small credit programs face several obstacles. The largest is loan defaults. Ban complained that many loan recipients migrate to urban areas after receiving loans. While commercial banks are able to transfer non-performing loans to other banking institutions, GX-RCU has to absorb the high financial costs itself. Annually, an average 20% of GX-RCU loans are not repaid on time and/or in full, with little improvement. These problems have been exacerbated by the general risks associated with the agricultural sector; this year alone, Guangxi has suffered harsh winter storms and flooding. Despite these challenges, the government has encouraged GX-RCU to increase support to poor farmers by 17%, without offering significant assistance.

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A Question of Status: NGO Operating Challenges

16. (SBU) Guangxi has not experienced the kind of growth in NGO microfinance institutions that other provinces in China have. However, two micro-lending NGOs that already operate in Guangxi hope to expand their reach. In 2000, World Vision, a Christian relief and development NGO headquartered in California, began a microfinance program in Guangxi's Baise municipality, which has been the scene of past land disputes. The program works with 220 households in six villages. Under it, households voluntarily invest their money into small credit programs, with the organization matching up to 70% of the group's investment. The money is then loaned out in amounts of up to RMB 3,000 (USD 441). The other NGO, the Guangxi Women's Federation's Poverty Alleviation Program, offers a small credit program to local women. From 1997 to 2000, the program assisted 150,000 households and distributed RMB 150 million (USD 22 million) in loans, ranging from RMB 1,000 to 5,000 per loan. Both organizations plan to expand in Guangxi either by volume of loan recipients, or by branching out, in cooperation with local government, to Ziyuan, Longsheng, Guilin, and Congzuo municipalities. (Note: The Women's Federation is a unique NGO because it was originally backed by the Communist Party of China; therefore, the Federation's activities are largely encouraged by local government. Many NGOs are normally prohibited from officially registering, and operate under the radar. End Note)

17. (SBU) NGOs not affiliated with the local government face many challenges in entering Guangxi's rural finance sector, the first of which is legal status. World Vision, for example, is legally registered in Hong Kong, not Guangxi. While Guangxi allows the World Vision to operate, the local government has assigned the Poverty Alleviation Office to keep close tabs on the organization's activities. Based on previous incidences of rural finance scandals in the 1980s, local government remains suspicious of NGO lending. As a result, World Vision is not allowed to fund-raise in China but must instead acquire its entire budget from overseas. Kelvin Yau, Deputy Director of World Vision China, told us that he is acutely aware of the delicacy of the relationship between his NGO and the local government and that World Vision keeps its operations limited in size to avoid raising concerns among local officials. For Yau, the balancing act is figuring out far he can push the envelope in expanding operations, without clear legal or financial parameters.

¶8. (SBU) In addition to legal status, World Vision has also faced the challenge of getting farmers interested in its credit. Yau says that many farmers within targeted villages are skeptical of the benefits of microfinance, especially from a foreign organization. Many in the countryside have become accustomed to free, sporadic aid offered by the local government, rather than conditional lending that requires a level of accountability to one's community. Farmers complain that conditions for receiving micro-loans are too harsh, such as interest rates that at 10-12% are higher than rates offered by banks. For NGOs, the challenge is educating farmers about the sustainable benefits of microfinance.

¶9. (SBU) Defaults have been a problem for World Vision too. It has a policy that if rates get too high in any one village, the NGO will cease operations there.

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Governmental Disconnect: Policy versus Practice
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¶10. (SBU) For the Guangxi government, microfinance is permitted because of the public benefit it provides but support is minimal. According to ABC-GX's Jiang, the local government has not provided any favorable policies or tax incentives to encourage microfinance. Thus far, reforms in Guangxi, including the expansion of commercial banking back into the rural sector, have been dominated by political motivations from above, rather than market forces and sound provincial financial policies. Financially speaking, GX-RCU's Ban commented that Guangxi's budget was limited in its ability to support microfinance programs, other than subsidizing interest rates, in spite of claims that the government had set aside more money for poverty alleviation efforts. In addition, Jiang says that commercial banks also face an "unsatisfactory" lending environment in the more risky rural sector without policy reforms to support the expansion there.

¶11. (SBU) Despite a lack of policy support, the local government and

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commercial banks have confidence in the rural sector's potential in the long term, according to Jiang, but the government plans to let the market be the driving force in the growth of rural finance. However, a major expansion of microfinance in Guangxi is unlikely without significant reforms that balance both political goals, and financial growth.

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